

Beyond Brexit: The UK’s proposed future relationship with Europe

August 2018

After repeated demands from both sides of the Channel, the UK Government has finally outlined its view of and aspirations for the future UK-EU trading relationship. On 12 July 2018, the UK Government published the long-awaited White Paper and formally called for an ‘Association Agreement’ (or more accurately, a series of agreements) which would take the UK out of the Single Market and the Customs Union but would tie the UK to a ‘common rule book’ with the EU governing trade in goods. Publication of the paper has generated heated political and industry reaction in both the UK and the EU27, but after months of political wrangling within Government, the UK finally has a position from which to negotiate.

Background

Article 50(2) of the Treaty of the European Union (TEU) specifically provides that the withdrawal agreement required under that article (the Article 50 Withdrawal Agreement) shall “take account of the framework” of the “future relationship” between the departing State and the EU. In addition, the UK’s European Union (Withdrawal) Act 2018 requires the Government to lay the framework of the future trading relationship before Parliament when it seeks approval for the Article 50 Withdrawal Agreement and that framework must include a statement that agreement in principle has been reached on the substance of the future relationship.

Publication of the blue print for the UK-EU future relationship had been delayed multiple times and although it was expected ahead of the June 2018 EU Council meeting, it was finally published following a UK cabinet meeting on 6 July 2018. There has been much political upheaval in the UK in response to the proposed plans. At the EU level, there has been no outright rejection of the proposals as a whole, although Michel Barnier has reiterated the EU’s commitment to the single market, and the indivisibility of its four freedoms, which appears to be at odds with key parts of the White Paper, particularly on the freedom of movement for workers. It has, however, been acknowledged that the White Paper provides a basis for continued discussions. This bulletin therefore considers the key elements of the future relationship agreements being proposed by the UK Government.

Free trade area for goods

The White Paper proposes the establishment of a free trade area for goods, including agri-food. The UK and the EU would maintain a “common rulebook” for goods including agri-food - effectively continuing existing regulatory and customs arrangements for manufacturing and agricultural products after the end of the transition period in December 2020. This will be achieved by the UK agreeing to be bound by EU rules, with a treaty-based commitment to “on-going harmonisation with EU rules on goods”.

The UK's proposal for a common rulebook would only cover those rules necessary to provide frictionless trade at the border. In the case of manufactured goods, this would encompass all rules that could be checked at the border, as they set the requirements for placing such goods on the market. The goal of such a proposal is to obviate the need for regulatory checks on the Irish border and prevent disruption to complex supply chains.

A new Facilitated Customs Arrangement has been proposed to remove the need for customs checks and controls between the UK and the EU as if in a combined customs territory, whilst enabling the UK to control tariffs for its own trade with the rest of the world. Tariffs, quotas and routine requirements for rules of origin for goods traded between the UK and the EU would be eliminated. The UK believes that this would ensure interoperability between UK and EU supply chains, removing the need for regulatory checks at the border.

Our Life Sciences team has considered the potential ramifications for that industry in [this](#) blog post which can be accessed via the Life Sciences [Hub](#).

Services and investment – a new arrangement

Whilst the proposals for the trade in goods seek to ensure as close a relationship as possible, the proposed approach for services is more nuanced. The White Paper proposes an arrangement that would include:

- general provisions to minimise the introduction of discriminatory and non-discriminatory barriers to the cross-border provision of services, with barriers only permitted where agreed upfront. The proposed arrangement would seek broad coverage across services sectors and modes of supply consistent with the requirements of the General Agreement on Trade in Services;
- the establishment of a system for the mutual recognition of professional qualifications that covers the same range of professions as the Professional Qualifications Directive (2005/36/EC), and includes those operating either on a permanent or a temporary basis across borders; and
- a new economic and regulatory arrangement for financial services.

Financial services

The White Paper acknowledges that when the UK leaves the EU and the single market it can no longer operate under the ‘passporting’ regime, as this is intrinsic to the Single Market of which it will no longer be a member. In a move away from the ‘mutual recognition’ model advocated by the UK Chancellor of the Exchequer Philip Hammond and regulators such as Andrew Bailey (CEO of the UK Financial Conduct Authority), the paper calls for a bilateral relationship concerning mutual market access based on a form of ‘enhanced equivalence’. This arrangement would be based on the principle of autonomy for each party on decisions relating to access to its market, with a bilateral framework of treaty-based commitments underpinning the operation of the relationship aimed at ensuring transparency, stability and co-operation.

The White Paper discusses the inadequacies of the existing third country regimes under EU law for integrated markets; namely, the lack of provision for institutional dialogue and supervisory co-operation, mediation and change processes as well as the large gaps in the scope of services and activities caught by those regimes. Given these inherent issues, the UK Government expects the new arrangement to include the following:

Expanded scope

It is proposed that the new arrangement encompasses a broader range of cross-border activities – presumably this would then capture activities such as banking and payment services – although the UK Government acknowledges that this arrangement cannot replicate the EU's passporting regime.

Mutual recognition under existing third country regimes

Given that the UK and the EU start from a position of identical rules and entwined supervisory frameworks, the UK proposes that there should be reciprocal recognition of equivalence under all existing third country regimes, taking effect at the end of the implementation period.

Constraints on autonomy

Whilst future determinations of equivalence would be an autonomous matter for the UK and EU, the White Paper suggests that the new arrangement should include provisions through the bilateral arrangement for:

- Common principles for the governance of the relationship – it is envisaged that the approach would be based on an evidence-based judgment of the equivalence of outcomes achieved by the respective regulatory and supervisory regimes. The UK and EU would set out a shared intention to avoid adopting regulations that produce divergent outcomes in relation to cross-border financial services.
- Extensive supervisory co-operation and regulatory dialogue –the White Paper suggest that there should be close supervisory co-operation concerning firms that pose a systemic risk or that provide significant cross-border services on the basis of equivalence (or both) and that there should be codified procedures for routine co-operation and for co-ordination in crisis situations. In terms of regulatory dialogue this would include the UK and EU being able to comment on each other's proposals at an early stage through a structured consultative process of dialogue at both a political and technical level.
- Predictable, transparent and robust processes – the UK envisages that some of these would be bilaterally agreed and treaty-based whilst others would be through autonomous measures of the parties. In terms of processes these would include: (i) a transparent assessment methodology for assessing equivalence which would make use of industry consultation; (ii) a structured withdrawal process which has an initial period of consultation on possible solutions prior to the establishment of clear timelines and notice periods (which are appropriate for the scale of change) before the withdrawal takes effect; and (iii) long term stabilisation with each side trying to avoid future changes that impact equivalence in new ways that could destabilise an established relationship.

The proposals outlined above are justified by explicit reference to interconnection and dependency, and backed by the (implicit) threat of disruption in the event of a no-deal Brexit (in particular a slowdown of inward credit flows into the EU). However, it should come as no surprise that Michel Barnier has rejected the idea that a new arrangement would be able to restrict the way in which EU regulators exercise their decision-making autonomy as regards equivalence determinations.

Civil justice co-operation

The UK Government's proposals on civil justice are consistent with the position it has put forward since the publication of its future partnership paper on civil judicial co-operation in August 2017. Specifically, the White Paper states that the UK will seek to participate in the Lugano Convention 2007 (the Convention on civil jurisdiction and judgments that currently applies between all EU Member States and Switzerland, Iceland and Norway). It also states that the UK Government is "keen to explore a new bilateral agreement with the EU, which would cover a coherent package of rules on jurisdiction, choice of jurisdiction, applicable law and recognition and enforcement of judgments in civil, commercial, insolvency and family matters" and that this would seek to build on the principles established in the Lugano Convention and subsequent developments at EU-level in civil judicial cooperation.

From a business perspective, this is good news. A mutual regime on civil jurisdiction and judgments, whether in the form of the Lugano Convention or an enhanced version of it, would maintain legal certainty and continuity and facilitate cross-border trade, thereby benefiting businesses in both the EU27 and the UK.

Data protection

As data protection continues to play an increasingly important role in the global economy and ensuring security, the White Paper highlights the need for continued co-operation between the UK and the EU in this cross-cutting area.

The importance of the continued exchange of personal data between the EU and UK, under the backdrop of strong privacy protections for data subjects, is reinforced. To achieve this, the UK government has proposed a two stage approach. The first step is to obtain an adequacy determination from the European Commission once the UK is no longer part of the EU. By way of background, the adequacy model is a mechanism that allows the European Commission to recognise a country outside the EU (known as a third country) as having an adequate level of protection of personal data to allow data to flow from the EU to recipients in that third country without additional safeguards, such as contractual solutions, to be put in place. Next, the government proposes going beyond the adequacy framework in two key respects:-

- a clear, transparent framework to facilitate dialogue, minimise data flow disruption and support the relationship between the EU and the UK to ensure stability with respect to the flow and protection of personal data; and
- joined up enforcement action, through the One Stop Shop, and continued co-operation between the UK Information Commissioner and the EU data protection authorities, presumably through the European Data Protection Board (EDPB). The White Paper cites the EU's developing thinking on cooperation with third countries and the recognition in the newly implemented General Data Protection Regulation that the European Commission and EU data protection authorities should work to agree international co-operation mechanisms with third countries in order to facilitate the global enforcement of data protection legislation. Although the UK's participation on the EDPB and, in particular, the One Stop Shop would certainly be ideal for clients, this would mean the EU moving into unchartered territory where it was treating the UK differently from other third countries. It remains to be seen if this is an acceptable proposal to the EU – current indications from Michel Barnier are that it is not.

Finally, the White Paper addresses the exchange of classified information for the purpose of common analysis and future cooperation, especially with respect to security. The UK and EU have been discussing a Security of Information Agreement (SoIA) on classified information to encourage this exchange. In addition to the SoIA, the White Paper refers to the need to exchange sensitive, but non-classified, information, which would be subject to a separate agreement.

Mobility and the impact on access to talent

While confirming that free movement rights will end from December 2020, the White Paper proposes a new “framework for mobility” with reciprocal arrangements for citizens to continue moving between the UK and EU for certain purposes. For workers, this would include visa-free travel for short-term business reasons (permitting paid work in specified circumstances in line with current business visa policy) and intra-corporate transfers based on current arrangements with non-EU countries, allowing UK and EU-based companies to train them, move them between offices and plants and to deploy any necessary expertise. Measures to help scientists and researchers, self-employed professionals, employees providing services, and investors are also being considered (but to permit movement on a more temporary basis).

Concessions will apply to Irish citizens, who can continue to move freely between Ireland and the UK (the Common Travel Area) and to citizens who arrive and are living in the UK (or in the EU, as the case may be) by the end of 2020, whose rights will be safeguarded.

More detail on the proposed framework should be provided by a separate white paper on immigration policy, expected later this year.

Governance and dispute resolution

The White Paper includes a series of proposals aimed at ensuring the future relationship functions properly. Among other things, it proposes:

- a Governing Body at leader and ministerial level, which will provide a forum to set the direction for the future relationship, discuss any changes and provide transparency and accountability;
- a Joint Committee, which will steer the development of the future relationship, manage and monitor implementation, resolve disputes and provide administrative functions, including dealing with:
 - proposed legislative change in areas where there is a common rulebook between the EU and the UK (which, among other things, would involve trying to agree on whether a proposed change could be incorporated into the relationship agreements and, where no agreement is reached, considering alternative options and/or “rebalancing measures” (eg compensation) or suspension of the relevant part of the relationship);
 - issues relating to equivalence in areas where equivalence has been agreed (which would involve trying to agree on whether an amended rule remained equivalent, considering alternative solutions where necessary, referring issues to independent arbitration where no agreement could be reached and, where rules were no longer equivalent, proposing “rebalancing measures”);
 - ensuring consistent interpretation of the relationship agreements by keeping under review the case law of the senior courts of the UK and the CJEU and acting to preserve consistency if significant divergences were found;
- Parliament-to-Parliament discussions;
- consultation over new legislative proposals in areas where there is a common rulebook;
- provisions outlining the implications of not complying with commitments under the relationship agreements and on how to deal with unforeseen events. In this context the White Paper suggests that the complaining party should be able to take proportionate, temporary and localised measures to mitigate any harm, including imposing financial penalties or the suspension of specific obligations; and
- the ability to refer disputes to independent arbitration including members from both parties, with the tribunal being able to refer questions on the interpretation of EU law to the CJEU in areas where there is a common rulebook, with the tribunal being required to resolve disputes in a way that is consistent with the CJEU’s interpretation.

The White Paper also suggests that, when interpreting provisions of national legislation intended to give effect to the agreements, the courts of each party could take into account the relevant case law of the other party and that, where the UK has agreed to retain a common rulebook, the UK’s courts would pay due regard to CJEU case law insofar as it was relevant.

Next steps

Given the time it has taken the UK Government to formulate its proposals, it is not surprising that EU negotiators and Member State governments are keen to be seen as constructive in their reactions. With only three months until both sides are meant to finalise the Article 50 Withdrawal Agreement and to produce a political declaration on the future relationship, thereby allowing sufficient time for both the UK and European Parliaments to complete the ratification process, negotiations will have to be productive and focused over the summer months.

Practical comment

Whilst clarification on the UK’s position as regards the future relationship is a positive step forward, the lack of granular detail so late in the Article 50 TEU withdrawal process is problematic. There have been suggestions that whilst still in office, David Davis and his team had been working on the text of the envisaged “Association Agreement”(or agreements); however, despite calls for publication, the text does not appear to be forthcoming. It is clear from the negotiations of the

Article 50 Withdrawal Agreement, that where a draft text can be formally published, it tends to form the basis from which negotiations flow.

Throughout the White Paper there is reference to the future relationship likely consisting of a number of separate agreements, each covering different elements of co-operation. The details of each individual agreement would be subject to negotiation, and the Government's position appears to be that some of these would be legally binding (for instance, components of the economic partnership such as a core Free Trade Agreement) while others would be based on political commitments. This approach would appear to mirror that adopted for the Swiss-EU relationship which has proved complex to manage due in part to the lack of one single agreement.

Financial services

In relation to financial services, although Michel Barnier has rejected the notion of EU regulators having their autonomous decision making restricted in relation to equivalence determinations, the UK's move away from the mutual recognition model to one of 'enhanced equivalence' is more aligned with the rhetoric seen over the last few months from Europe. Prior to the March 2018 EU Council summit, a leaked version of the negotiating guidelines was circulated which was reported to include financial services for the first time. Press coverage suggested that in that draft, a new "Annex IV" was included which dealt specifically with financial services and stated that the aim in talks should be market access for UK-based financial firms via 'reviewed and improved equivalence mechanisms'. Whilst it was reported that financial services were discussed at the summit, the new Annex IV was not included in the final guidelines. On 10 July, in a speech at the European American Chamber of Commerce, Michel Barnier questioned why the current equivalence system, "which works well, including for the US industry, would not work for the UK".

Understandably, however, the Government's change in approach has not been welcomed by the financial services industry which has argued vehemently beside the Chancellor of the Exchequer and UK regulators for a future relationship based on mutual recognition.

Your Allen & Overy contacts



Karen Birch
PSL Counsel
Litigation
+44 20 3088 3737
karen.birch@allenoverly.com



David Campbell
Partner
Banking
+44 20 3088 4758
david.campbell@allenoverly.com



Damian Carolan
Partner
Banking
+44 20 3088 2495
damian.carolan@allenoverly.com



Lydia Challen
Partner
Tax
+44 20 3088 2753
lydia.challen@allenoverly.com



Angela Clist
Partner
ICM
+44 20 3088 2437
angela.clist@allenoverly.com



Richard Cranfield
Partner
Corporate
+44 20 3088 3200
richard.cranfield@allenoverly.com



Jennifer Cresswell
PSL Counsel
ICM
+44 20 3088 4872
jennifer.cresswell@allenoverly.com



Jane Finlayson-Brown
Partner
Corporate
+44 20 3088 3384
jane.finlayson-brown@allenoverly.com



Sarah Garvey
Counsel
Litigation
+44 20 3088 3710
sarah.garvey@allenoverly.com



Oonagh Harrison
Senior PSL - Brexit
Management
+44 20 3088 3255
oonagh.harrison@allenoverly.com



Matthew Hartley
Partner
ICM
+44 20 3088 2824
matthew.hartley@allenoverly.com



Sarah Henchoz
Partner
Litigation
+44 20 3088 4810
sarah.henchoz@allenoverly.com



Etay Katz
Partner
Banking
+44 20 3088 3823
etay.katz@allenoverly.com



Anne Kirkwood
Senior PSL
Corporate
+44 20 3088 2165
anne.kirkwood@allenoverly.com



Bob Penn
Partner
Banking
+44 20 3088 2582
bob.penn@allenoverly.com



James Roe
Partner
Corporate
+44 20 3088 4637
james.roe@allenoverly.com



Daniel Shurman
Partner
ICM
+44 20 3088 2855
daniel.shurman@allenoverly.com



Maria Stimpson
Partner
Corporate
+44 20 3088 3665
maria.stimpson@allenoverly.com



Kate Sumpter
Partner
Banking
+44 20 3088 2054
kate.sumpter@allenoverly.com



Matthew Townsend
Partner
Corporate
+44 20 3088 3174
matthew.townsend@allenoverly.com

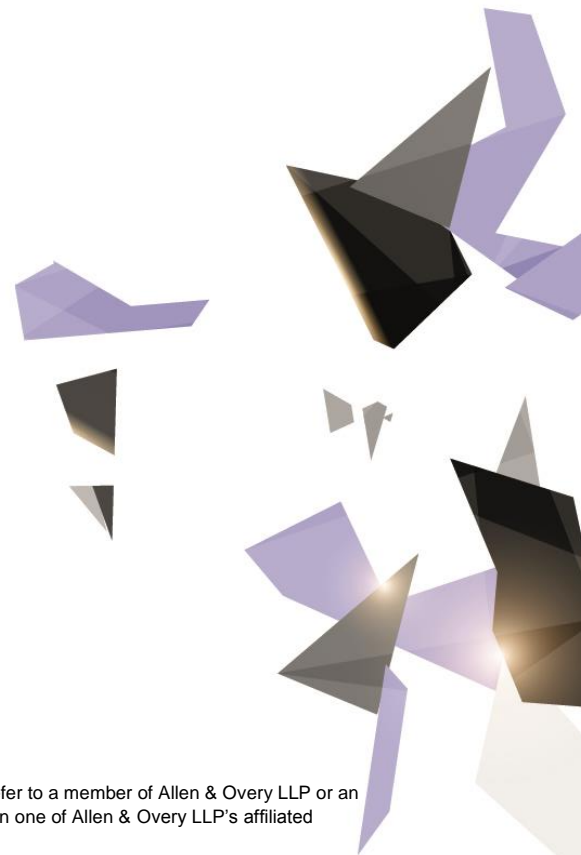


Richard Tredgett
Partner
ICM
+44 20 3088 2467
richard.tredgett@allenoverly.com



Elizabeth Wall
PSL Cnsl/Head KH, Global Corp
Corporate
+44 20 3088 3075
elizabeth.wall@allenoverly.com

If you would like to discuss the issues raised in this paper in more detail, please contact any of the experts above or your usual Allen & Overy contact.



Allen & Overy means Allen & Overy LLP and/or its affiliated undertakings. The term **partner** is used to refer to a member of Allen & Overy LLP or an employee or consultant with equivalent standing and qualifications or an individual with equivalent status in one of Allen & Overy LLP's affiliated undertakings. | MKT:7450400.1